

MINUTES
BOARD OF TRUSTEES OF THE
PUBLIC EMPLOYEES' RETIREMENT FUND
143 West Market Street, Suite 500
Indianapolis, Indiana 46204
October 20, 2006

REGULAR SESSION

Board Members Present

Ken Cochran, Chair
Tony Armstrong, OMB Director Designee
Kathy Ettensohn
Regina Overton
Matt Murphy
Bob Welch

Board Members Absent

Others Present

Cristy Wheeler, Executive Director, Teacher's Retirement Fund
Paul Joyce, Deputy State Examiner, State Board of Accounts
Curt Smith, Strategic Investment Solutions, Inc.
Iliana Nikolova, Mercer Investment Consulting
Doug Kryscio, Mercer Investment Consulting
Doug Todd, McKready & Keene
Elaine Beaty, McKready & Keene
Teresa Wesner, Purdue University
Dan Hackler, State Personnel

PERF Staff Present

David Adams, Executive Director
Terry Magid, Chief Operating Officer & Deputy Director
Dave Huffman, Chief Technology Officer & Deputy Director
Andrea Unzicker, General Counsel
Will Frayer, Staff Attorney
Shawn Wischmeier, Chief Investment Officer
Kate Cooper, Director of Retirement Services
Jeff Huston, Director of Communications
Patricia Bush, Director of Finance
Erin Hankins, Executive Assistant, to David Adams

Meeting called to order at 1:00 by Chairman Cochran.

I. Approval of Minutes

MOTION duly made and carried to approve the minutes from the August 18, 2006 board meeting.

Proposed by: Matt Murphy
Seconded by: Kathy Ettensohn
Votes: 6 in favor, 0 opposed, 0 abstentions

II. Old Business

- **Audit Update**

David Adams introduced Paul Joyce to the Board. Mr. Joyce is the Deputy State Examiner of the State Board of Accounts (SBOA). Mr. Joyce stated that the SBOA is prepared to deliver an unqualified financial opinion to the Public Employees' Retirement Fund (PERF). He noted that the culture has changed for the better at PERF and that he was pleased with the assistance offered by the PERF staff and management. He thanked Mr. Adams and Terry Magid for their cooperation.

- **Investment Manager Update**

Shawn Wischmeier provided the board with an investment manager update. PERF staff and Mercer recently visited Hughes Capital Management (HCM). The firm has made good progress. PERF staff and Mercer will continue to monitor the firm, as with all managers, over the next year. Staff and Mercer will proceed with the planned move to the Lehman Aggregate benchmark as approved. HCM will remain a manager in good standing in PERF's portfolio.

III. Executive Director Report

David Adams reviewed PERF's quarterly scorecard measures. PERF's quarterly measures are featured as the example agency in Governor Daniels' six-month performance report (January 2006 – June 2006). Mr. Adams reviewed the first quarter goals of fiscal year 2007 and highlighted the second quarter goals.

- Board Governance Education
- Implement Budgeting Process
- Release of the Annual Report
- Reaching out to 100% of the members who are eligible to retire.

- Employer Training Event.
- Strategic Study Contract
- PERF Interactive service credit to employers retirement

IV. **New Business**

- **Benefits**

Proposed Changes to Service Credit

Mr. Adams introduced Will Frayer to the Board. Mr. Frayer is the Staff Attorney for PERF. He received the prestigious Governor's public service award and was nominated for Indy's Best and Brightest award. Mr. Frayer began by detailing the problems surrounding service credit. Current Indiana Administrative Code provision states "Total service credit shall be computed in whole months only. Any period of less than thirty (30) days in such total will not count as creditable service." Currently employers report contributions and service quarterly. PERF's record keeping system was designed to support quarterly reporting and administration. Disconnect between law and reality produces administrative burdens. Administering the "30-day rule" results in manual service credit calculations at retirement and researching old records by both PERF and participating employers.

Mr. Frayer introduced Teresa Wesner, the Benefits Manager at Purdue University and Dan Hackler, the Deputy Director for the Indiana State Personnel Department. Ms. Wesner described to the board the challenges Purdue faces when calculating service credit. Ms. Wesner has three full-time employees working on service credit. She informed the board that she is very pleased with the positive changes happening at PERF. Mr. Hackler spoke to the board and echoed Ms. Wesner's comments. He estimates that the State of Indiana spends 200 man hours a month calculating service credit.

After Ms. Wesner and Mr. Hackler spoke, Mr. Frayer continued explaining the benefits of amending the current administrative code.

- Fewer information requests from PERF.
- No longer necessary to devote time to researching law quarters.
- Reduction in time devoted to PERF matters will allow staff to concentrate on other important issues
- Less delay between last check from employer and first benefit check from PERF

Ken Cochran asked Mr. Frayer why the law was originally passed. Mr. Frayer stated that is not known at this time why the law was passed.

MOTION duly made and carried to approve Resolution No. 06-05.

<i>Proposed by:</i>	<i>Tony Armstrong</i>
<i>Seconded by:</i>	<i>Regina Overton</i>
<i>Votes:</i>	<i>6 in favor, 0 opposed, 0 abstentions</i>

Policy Review

Mike Henning explained to the board the recommended policy revisions. The objective was to review and update PERF's personnel policies to be clearer, more comprehensive and designed to be supportive of organizational values and expectations while aligning with the State of Indiana's policies in important areas. Mr. Henning reviewed the proposed changes with the board and recommended that the policies be reviewed every two years.

MOTION duly made and carried to approve the recommended policy revisions and to review them every two years.

<i>Proposed by:</i>	<i>Matt Murphy</i>
<i>Seconded by:</i>	<i>Kathy Ettensohn</i>
<i>Votes:</i>	<i>6 in favor, 0 opposed, 0 abstentions</i>

- **Investments**

Investments Update

Shawn Wischmeier provided the board with an Investments update. The CRIF returned 3.7% for the quarter. Mr. Wischmeier stated that 79% of PERF's active managers beat their three year benchmark.

Private Equity Recommendations

Mr. Wischmeier discussed three private equity commitments that staff recommends the board approve. These recommendations would increase total private equity commitments from 24% to 31% of the desired commitment level.

The first investment proposal is to Cerberus Institutional Investors. Cerberus is a \$6 billion global buyout fund focused on taking control of distressed companies with good historical revenues.

Cerberus then adds value by supplying needed capital and improving management/operational capabilities. Cerberus has three previous, successful funds with expected new IRR's that range from 15 to 30%. Cerberus is not a standard private equity firm in that it employs over 285 people and will close relatively fewer deals per year. The management is focused on utilizing significant resources to drive value out of companies or industries. The Investments staff recommends that the Board approve up to a \$75 million commitment to Cerberus Institutional Investors, Series Four pending due diligence and document review by legal counsel. Additionally, SIS and the Investment staff recommends that the Board give approval for up to two consecutive one year term extensions as dictated in the fund's offering memorandum.

MOTION duly made and carried to approve up to a \$75 million commitment to Cerberus Institutional Investors Series Four and to approve two consecutive one year term extensions pending final due diligence and document review by legal counsel.

<i>Proposed by:</i>	<i>Matt Murphy</i>
<i>Seconded by:</i>	<i>Kathy Ettensohn</i>
<i>Votes:</i>	<i>6 in favor, 0 opposed, 0 abstentions</i>

The second investment proposal is Energy Capital Partners I (ECP I). A \$1.5 billion dollar fund, ECP I is a first time fund that has been formed by a seasoned team with a demonstrated track record. ECP is in the final stages of closure of its first fund and has a long list of other public and private investors already committed. ECP will focus on energy infrastructure investments in areas like power generation, electric transmission, gas storage, and electric and gas transmission. ECP is focused on adding value without taking commodity risk. The Investments staff recommends that the Board approve up to a \$75 million commitment to Energy Capital Partners I, LP pending final due diligence and document review by legal counsel. Additionally, SIS and the Investment staff recommends that the Board give approval for up to three consecutive one year term extensions as dictated in the fund's offering memorandum.

MOTION duly made and carried to approve up to a \$75 million commitment to Energy Capital Partners I, LP pending due diligence and document review by legal counsel and for three potential one year term extensions.

<i>Proposed by:</i>	<i>Matt Murphy</i>
<i>Seconded by:</i>	<i>Kathy Ettensohn</i>
<i>Votes:</i>	<i>6 in favor, 0 opposed, 0 abstentions</i>

The third investment proposal is Hellman & Friedman Capital Partners VI (HF VI). Hellman & Friedman Capital Partners VI is raising an \$8 billion global buyout fund focused on taking control and non-control positions in good private companies that have the potential to be great. HF focuses on companies with strong, predictable revenue and earnings growth. The five previous HF funds have returned a net 27% to investors to date. The Investments staff recommends that the Board approve up to a \$75 million commitment to Hellman & Friedman Capital Partners VI pending due diligence and document review by legal counsel. Additionally, SIS and the Investment staff recommends that the Board give approval for up to three consecutive one year term extensions as dictated in the fund's offering memorandum.

MOTION duly made and carried to approve up to a \$75 million commitment to Hellman & Friedman Capital Partners VI pending due diligence and document review by legal counsel and for three potential one year term extensions.

<i>Proposed by:</i>	<i>Matt Murphy</i>
<i>Seconded by:</i>	<i>Kathy Ettensohn</i>
<i>Votes:</i>	<i>6 in favor, 0 opposed, 0 abstentions</i>

Mr. Wischmeier informed the board that Cristy Wheeler was present at the board meeting. Ms. Wheeler is the Executive Director of the Teacher's Retirement Fund (TRF). Based on TRF's approval, Ms. Wheeler is requesting contributing up to \$50 million in the funds portion of the Indiana Investment Fund I. Mr. Wischmeier explained the benefits of allowing TRF join the fund.

- PERF would see a reduction in fees
- PERF would have better leverage on funds
- PERF would remain in charge of the fund

MOTION duly made and carried to approve the contribution of up to \$50 million in the "funds" portion of the Indiana Investment Fund I by TRF.

<i>Proposed by:</i>	<i>Bob Welch</i>
<i>Seconded by:</i>	<i>Matt Murphy</i>
<i>Votes:</i>	<i>6 in favor, 0 opposed, 0 abstentions</i>

Administrative Issues

PERF entered into contracts with a pool of transition managers in 2004 to provide portfolio transition services for moving large or complicated portfolios from one manager to another. This service

reduces the overall cost to the fund in terms of performance and transactions costs. The Investment staff reviewed the current pool of Transition Management service providers and determined that it would be appropriate at this time to refresh our slate of managers.

An RFP was issued in June to update our slate of managers. No business will be awarded as a result of this RFP, but the contract will give selected firms the right to bid on future transition services (known as an Optional-Use Contract). There are eleven responses to the RFP and eight are recommended for approval. The eight include:

- Northern Trust Global
- Barclay's Global Investors
- State Street Corporation
- Blackrock Investment Management
- BNY Global Transition Management
- Credit Suisse
- JP Morgan Transition Management
- Frank Russell Securities, Inc.

MOTION duly made and carried to approve the eight service providers for transition management services, subject to final contact negotiations and review by legal counsel.

Proposed by:
Seconded by:
Votes:

Tony Armstrong
Kathy Ettensohn
6 in favor, 0 opposed, 0 abstentions

- **Audit & Budget**

Financial Update

Mr. Adams introduced Patricia Bush to the Board. Ms. Bush is the new Director of Finance for PERF. Ms. Bush reviewed the financials with the board. She explained to the board that all PERF managers will be expected to manage their own budgets on a monthly basis. Mr. Adams pointed out that this is an evolving and learning process for the PERF staff. PERF managers will monitor their actual spending versus their budget to ensure fiscal responsibility and accountability. The Finance department will generate a monthly "Actual vs. Budget" report for each cost center and provide a monthly variance report to department heads by the 12th business day. The long term objective is to prepare a more accurate budget and to forecast early for next year's expenses.

- **Strategic Road Map Update**

Mr. Adams introduced David Huffman to the Board. Mr. Huffman explained that PERF currently uses SIRIS. SIRIS is a computer system that was built on a platform that will not be supported after 2007. SIRIS currently has several issues:

- SIRIS security structure not robust
- Current architecture is not web friendly
- No cost effective path away from quarterly processing
- System was poorly implemented
- Data quality & data validation is poor

The system has become costly to maintain. The majority of PERF's information technology dollars go to maintaining SIRIS. Mr. Huffman explained that the system will need to last PERF for at least 3-5 years. Mr. Cochran asked why was PERF's system was so complicated. Mr. Adams explained that PERF is unique because they handle both defined contributions and defined benefits. Most systems handle one or the other, but not both. PERF is reviewing options to solve the issues surrounding SIRIS. They are the following:

- Continue trying to fix the current system
- Outsource one or both DB & DC
- Procure a new system and modify it to our needs
- Specify & develop a new system
- Some combination of the above

PERF is issuing a RFP to select consultant to assist PERF in developing a five year technology plan and road map. PERF will present the results and recommendation at the February 2007 board meeting.

V. Date of Next Meeting

November 6, 2006 at 8am

VI. Adjournment

Adjourned at 3:43pm.